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No. 76-790

In the Supreme Court of the United States

OCTOBER TERM, 1976

MARVIN MILLER, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

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OPINIONS BELOW

The district court did not issue a written opinion. The opinion of the court of appeals (Pet. App. A) is reported at 545 F. 2d 1204.

JURISDICTION

The judgment of the court of appeals was entered on November 10, 1976. The petition for a writ of certiorari was filed on December 10, 1976. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTIONS PRESENTED

1. Whether proof that petitioner diverted to his own use $860,000 of the gross receipts of his wholly-owned corporation, that he did not report such sums on his tax returns, that his basis in the stock of the corporation had

been only $128,000, and that his stated salary was low in relation to his management responsibilities, was sufficient to support his conviction for income tax evasion and filing of a false return, even though there was no evidence that the corporation had any earnings and profits.

2. Whether the mailing of a false federal or state income tax return constitutes mail fraud in violation of 18 U.S.C. 1341.

STATEMENT

After a trial in the United States District Court for the Central District of California, petitioner was found guilty of six counts of mail fraud, in violation of 18 U.S.C. 1341; five counts of income tax evasion, in violation of 26 U.S.C. 7201; seven counts of filing a false income tax return, in violation of 26 U.S.C. 7206(1); and four counts of filing a false claim against the United States, in violation of 18 U.S.C. 287 (Pet. App. A 1-3, 5). The trial court sentenced him to concurrent three-year prison terms on each of 11 counts, and concurrent three-year prison terms on the remaining 11 counts, with the term in the second group of counts to run consecutively with the term in the first group of counts. The court also specified, in accordance with 18 U.S.C. 4208(a)(2), that petitioner could become eligible for parole at such time as the parole board might determine (R.T. 1301).[1]

The pertinent facts are as follows: During the period January 1, 1968, to June 1, 1970, petitioner operated Covina Publications, Inc., the business of which was the sale of "adult" books, films and devices to the general public by mail order and to wholesale distributors.

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[1] "R.T." refers to the reporter's transcript.

Petitioner dominated and controlled Covina. He purchased all of Covina's issued stock for $128,000, and the stock was held in the names of his wife and four children (Pet. App. A 2-3).

The evidence at trial showed that for Covina's taxable year ended May 31, 1969, approximately $562,000 of receipts were not recorded as sales on its corporate books or reported on the corporate tax returns filed by petitioner. For Covina's taxable year ended May 31, 1970, approximately $298,000 likewise was omitted. The evidence further showed that most of the omitted receipts were deposited in various business and personal bank and savings accounts established by petitioner under various names, including those of his wife and children. The receipts diverted by petitioner were recorded on Covina's books either as loans from petitioner or from banks, or as intercompany transfers (Pet. App. A 3-4).

During the period May 31, 1968 to May 31, 1970, petitioner received, in addition to his salary, various economic benefits from Covina. For example, Covina paid virtually all of petitioner's personal obligations. The total of such payments was in excess of $197,000, and was recorded on Covina's books as repayment of loans. Petitioner did not report any of these payments on his tax returns (Pet. App. A 4).

At trial, petitioner admitted that he had instructed his accountant to "scramble" the corporate books. However, he later testified that his sole purpose in distorting the corporate books was to conceal his income from his creditors and not to cheat the government (Pet. App. A 4).

For its taxable year ended May 31, 1969, Covina reported a net loss of $216,000. At trial, an expert witness testified on behalf of petitioner that the loss for that year should have

been $681,000. For its taxable year ended May 31, 1970, Covina reported a net loss of $697,000 (Pet. App. A 4).

ARGUMENT

1. Petitioner argues (Pet. 6-13) that he was improperly convicted of tax evasion and filing false income tax returns because the amounts of Covina's gross receipts that he diverted to his own use could not be taxed to him as dividends in the absence of any evidence that Covina had "earnings and profits" within the meaning of Section 316 of the Internal Revenue Code of 1954 (26 U.S.C.). But the existence of earnings and profits was not an indispensable element of proof of petitioner's offenses. The court of appeals agreed with "the trial court's holding that the $197,000.00 of diverted funds constituted additional salary to the [petitioner]" (Pet. App. A 15). Since additional salary was taxable to petitioner even if Covina had no earnings and profits, petitioner was properly convicted of tax evasion and filing false income tax returns.

In support of the conclusion that petitioner received $197,000 of additional salary, the court of appeals noted that the trial judge found petitioner's set salary to be too small given his responsibilities and the volume of the business he directed (Pet. App. A 15). Moreover, the amounts were not recorded on the corporate books as returns of capital, as petitioner contended, but as repayments of loans which were shown to be non-existent. Since petitioner admitted that he ordered the "scrambling" of the corporate books, the trial judge was amply justified in rejecting petitioner's claimed defense that the payments were returns of capital.

It is true that if Covina had no earnings and profits, the $860,000 diverted to petitioner would not have been taxable as a dividend. The payments instead would have been

treated as a return of capital. But the amount by which a return of capital exceeds a taxpayer's basis is taxable at capital gains rates. See Section 301(c)(3) of the Code. Petitioner's basis in the Covina stock was only $128,000 (see Pet. App. A 6, n. 7). Thus even under his theory he would have recognized over $700,000 in capital gains. Since petitioner failed to report any part of this amount, he was guilty of tax evasion and of filing a false return once he filed his tax return omitting the payment from income. See *Sansone* v. *United States*, 380 U.S. 343, 354; *United States* v. *Swallow*, 511 F. 2d 514, 521 (C.A. 10), certiorari denied, 423 U.S. 845.

2. Since petitioner's conviction stands even in the absence of earnings and profits of Covina, *a fortiori* it was not necessary for the prosecution to present evidence as to whether such earnings and profits existed. In any event, contrary to petitioner's claim (Pet. 6-8), there is no conflict of decisions on the question of the burden of proof with respect to earnings and profits. When the existence of earnings and profits is a necessary element of the offense, the ultimate burden of proof rests with the government. But where, as here, a shareholder diverts corporate receipts to his own use, the decision below correctly held that the government established a *prima facie* case of income tax evasion and that petitioner had the burden of coming forward with the defense that the amounts were not taxable, either because the corporation had no earnings and profits or for some other reason. Accord: *Davis* v. *United States*, 226 F. 2d 331 (C.A. 6), certiorari denied, 350 U.S. 965; *Hartman* v. *United States*, 245 F. 2d 349, 353 (C.A. 8); *United States* v. *Goldberg*, 330 F. 2d 30, 38 (C.A. 3), certiorari denied, 377 U.S. 953.

The burden of coming forward in such a case with evidence that there were no earnings and profits is no

different than the burden of refuting the government's net worth computation in a criminal tax prosecution. In that connection, this Court in *Holland* v. *United States*, 348 U.S. 121, 138-139, observed:

> Nor does this rule shift the burden of proof. The Government must still prove every element of the offense beyond a reasonable doubt though not to a mathematical certainty. The settled standards of criminal law are applicable to net worth cases just as to prosecutions for other crimes. Once the Government has established its case, the defendant remains quiet at his peril.

None of the cases cited by petitioner (Pet. 6-7) are in conflict with the decision below. As the court of appeals correctly observed (Pet. App. A 11, n. 11), *United States* v. *Leonard*, 524 F. 2d 1076 (C.A. 2), certiorari denied, 425 U.S. 958, is in accord with its decision and does not adopt petitioner's contention that the government must prove the existence of earnings and profits. Indeed, in upholding the conviction in *Leonard*, the Second Circuit stated: "Although the ultimate burden of persuasion remains with the Government, Leonard did not introduce sufficient evidence of an absence of earnings or profits to warrant submission to the jury of a claim [to that effect]" (524 F. 2d at 1083).[2]

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[2]Neither *Currier* v. *United States*, 166 F. 2d 346 (C.A. 1), nor *Bernstein* v. *United States*, 234 F. 2d 475 (C.A. 5), certiorari denied, 352 U.S. 915, supports petitioner's argument that the government must initially come forward with proof of the existence of earnings and profits. In upholding a tax evasion conviction in similar circumstances, the court in *Currier* did not address the question of the burden of coming forward but simply recognized that dividends are taxable only if paid out of earnings and profits (166 F. 2d at 348). *Bernstein* likewise is inapposite. There, the court rejected the defendant's efforts to reduce the corporate earnings and profits by the amount of a fraud penalty that the Commissioner subsequently imposed (234 F. 2d at 482).

3. Petitioner also contends (Pet. 13-14) that the mailing of false federal and state income tax returns does not constitute mail fraud under 18 U.S.C. 1341. But as the court of appeals pointed out (Pet. App. A 16, n. 17), other circuits also have upheld convictions under 18 U.S.C. 1341 for mailing false tax returns. *United States* v. *Flaxman*, 495 F. 2d 344 (C.A. 7), certiorari denied, 419 U.S. 1031; *United States* v. *Mirabile*, 503 F. 2d 1065 (C.A. 8), certiorari denied, 420 U.S. 973. See also *United States* v. *Brewer*, 528 F. 2d 492 (C.A. 4). Contra: *United States* v. *Henderson*, 386 F. Supp. 1048, 1050-1054 (S.D. N.Y.).

Moreover, the fact that a particular fraudulent scheme involving use of the mails also violates another federal statute has been held not to be a bar to prosecution under the mail fraud statue. *Pereira* v. *United States*, 347 U.S. 1, 8-9 (National Stolen Property Act); *Edwards* v. *United States*, 312 U.S. 473, 483-484 (Securities Act of 1933); *United States* v. *Brewer, supra*, 528 F. 2d at 497-498. Nothing in the broad language of 18 U.S.C. 1341—"any scheme or artifice to defraud"—suggests that Congress intended to exclude mailing a false federal or state tax return from its coverage.

CONCLUSION

For the reasons stated, the petition for a writ of certiorari should be denied.

Respectfully submitted.

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